

**REPORT OF EXAMINATION**  
**UNIGARD INSURANCE COMPANY**

**Bellevue, Washington**

**December 31, 1996**



States Participating

Washington

**CHIEF EXAMINER'S AFFIDAVIT**

I hereby certify that the attached Report of Examination shows the financial condition and affairs of **UNIGARD INSURANCE COMPANY** of Bellevue, Washington as of December 31, 1996.

\_\_\_\_\_  
JAMES T. ODIORNE, CPA, JD  
Deputy Insurance Commissioner  
Acting Chief Examiner

\_\_\_\_\_  
Date

# UNIGARD INSURANCE COMPANY

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## UNIGARD INSURANCE COMPANY

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**UNIGARD INSURANCE COMPANY**

Bellevue, Washington  
June 20, 1997

Hon. Josephine W. Musser  
Commissioner, Wisconsin Insurance Dept.  
Chair, NAIC Financial Condition (EX4)  
121 E. Wilson  
Madison, Wisconsin 53707-7873

Hon. Marianne K. Burke  
Director, Alaska Division of Insurance  
NAIC Secretary, Western Zone  
P.O. Box 110805  
Juneau, Alaska 99811-0805

Hon. Deborah Senn  
Commissioner, Washington Insurance Department  
Insurance Building AQ-21  
Olympia, Washington 98504-0255

Dear Commissioners:

In accordance with your instructions and in compliance with the statutory requirements of Chapter 48.03 RCW, an examination was made of the corporate affairs and financial records of

**UNIGARD INSURANCE COMPANY**

of

Bellevue, Washington

hereinafter referred to as the "Company" or "UIC," at its home office located at 15805 NE 24th Street, Bellevue, Washington 98008-2409.

The Report of Examination is respectfully submitted showing the condition of the Company as of December 31, 1996.

**SCOPE OF EXAMINATION**

Per RCW 48.03.010, the examination covered the five-year period from January 1, 1991 through December 31, 1995 and was carried forward through December 31, 1996. Concurrently, the examiners conducted the examination of the Company's subsidiary, Unigard Indemnity Company or "UID." Occasionally, reference to "the Companies" indicates that the items or discussion is equally applicable to the Unigard Insurance Company and Unigard Indemnity Company. The examiners from the states of Nevada and Washington examined the Company as of December 31, 1990. No NAIC Zone examiners participated in the current examination.

The examination followed the statutory requirements contained in the Washington Insurance Laws and the guidelines prescribed in the NAIC Financial Condition Examiner's Handbook. UIC's operating procedures and financial records were reviewed as considered necessary to ascertain the financial condition of the Company and conformity with related laws. These matters are discussed in various sections of the report. The examination included identification and disposition of material transactions and events occurring subsequent to December 31, 1996, and a limited review of market conduct issues.

**UNIGARD INSURANCE COMPANY**

**INSTRUCTIONS**

The examination detected no violations of Regulation or Law that require instructions to the Company.

## **UNIGARD INSURANCE COMPANY**

### **COMMENTS AND RECOMMENDATIONS**

The Company failed to correctly complete the annual statement line, “Premiums, agents’ balances and installments booked but deferred and not yet due.” The Company should book the actual amount rather than estimated amount, in accordance with NAIC annual statement instructions.

## **UNIGARD INSURANCE COMPANY**

### **HISTORY**

Unigard Insurance Company, the lead carrier of the Unigard Insurance Group, was incorporated as Northwestern Security Insurance Company on September 29, 1960 under the laws of the state of Washington. It began business on September 30, 1960. On September 14, 1968, UIC adopted its present name.

On December 31, 1981, all issued stock passed (as a surplus contribution) from Unigard Mutual Insurance Company, to its downstream holding company, Unigard, Inc. Effective September 30, 1984, Unigard Mutual completed a plan of demutualization. It changed its name to Unigard Security Insurance Company (USIC) at the same time Hanseco Insurance Company acquired USIC. On December 31, 1984, John Hancock Property and Casualty Holding Company obtained ownership of USIC. John Hancock Mutual Life Insurance Company indirectly owned John Hancock Property and Casualty Holding Company.

On August 9, 1990, the Company's Board of Directors approved the transfer of 100% ownership of Unigard Indemnity Company (UID) from Unigard, Inc. to UIC. Effective July 1, 1993, John Hancock Property and Casualty Holding Company sold to Winterthur U.S. Holdings, Inc., 100% of the stock of USIC's wholly owned subsidiary, Unigard, Inc., and its wholly owned subsidiaries: UIC, UID, Unigard Service Corporation and Unigard Service Corporation of California. Winterthur U.S. Holdings, Inc. is a wholly owned subsidiary of Winterthur Swiss Insurance Company of Switzerland.

### **CAPITAL AND SURPLUS**

The original authorized capital of the Company was \$1,000,000 which consisted of 10,000 shares of common capital stock with par value of \$100 per share. Unigard Mutual Insurance Company, also known as Unigard Security Insurance Company (USIC) subscribed and purchased all the authorized stock at \$300 per share for a total of \$3,000,000 with allocation of \$1,000,000 to paid up capital and \$2,000,000 to paid in surplus. On September 30, 1985, USIC contributed \$5,100,000 capital to Unigard, Inc., which in turn contributed the same amount to the Company.

On May 8, 1986, the Board of Directors approved the increase of capital stock from \$1,000,000 to \$2,500,000. The \$1,500,000 was transferred from paid in surplus to capital stock.

On August 9, 1990, the Board of Directors approved a resolution transferring the 100% ownership of UID from Unigard, Inc. to the Company and declaring USIC's contribution of \$10,000,000 of capital assets to the Company. On November 30, 1990 Unigard, Inc. transferred stock ownership of UID to the Company. On December 21, 1990, USIC contributed \$10,000,000 to the Company which increased gross paid in surplus to \$28,482,063.

On December 15, 1993, Unigard, Inc. contributed \$66,071,508 to the Company. This transfer increased gross paid in surplus to \$94,053,571. On November 30, 1994, Unigard, Inc. contributed \$25,000,000 to the Company which increased gross paid in surplus to \$119,053,571.

Currently, the authorized capital of the Company is \$3,000,000 consisting of 30,000 common shares at \$100 par value per share. All authorized shares are outstanding.



## UNIGARD INSURANCE COMPANY

### MANAGEMENT

#### Board of Directors

Article I, Section 1 of the Bylaws state that the business affairs of the Company shall be conducted by a Board of not less than seven (7) nor more than seventeen (17) directors. The directors are to be elected at each annual shareholders' meeting and are to hold office for one year.

The following directors, officers and committee members are serving the Company as of December 31, 1996:

<u>Directors</u>	<u>Principal Business Affiliation</u>	<u>Residence</u>
Dr. Hans-Rudolf Stucki	Gen. Manager, North America Dept. Winterthur Swiss Insurance Group	Winterthur, Switzerland
Laurence P. O'Connor	Chairman, President & CEO Unigard Insurance Group	Bellevue, WA
Dale E. Abbrederis	Sr. Vice President & CFO Unigard Insurance Group	Bellevue, WA
Mary K. Dawson	Vice President, Personal Lines Unigard Insurance Group	Bellevue, WA
Nelson A. Habenicht	Vice President, Marketing Unigard Insurance Group	Issaquah, WA
Cheryl L. Lang	Vice President, Human Resources Unigard Insurance Group	Redmond, WA
Gordon S. McLaren	Vice President, Commercial Lines Unigard Insurance Group	Redmond, WA
Paul B. Swank	Vice President, Claims Unigard Insurance Group	Issaquah, WA

## UNIGARD INSURANCE COMPANY

### **Elected Officers**

Article I, Section 2 of the Bylaws provide that the following officers of the Company shall be elected by the Board of Directors: Chairman of the Board, President, Executive Vice President, such number of Senior Vice Presidents, and Vice Presidents as the Board may determine, and General Counsel. Section 3 provides that the Chief Executive Officer may from time to time designate a Controller, Treasurer, Secretary and any number of Assistant Vice Presidents and Assistant Secretaries.

#### **Name**

#### **Title**

Laurence P. O'Connor	Chairman of the Board, President & Chief Executive Officer
Dale E. Abbrederis	Senior Vice President & Chief Financial Officer
Mary K. Dawson	Vice President, Personal Lines
Jerry L. Epler	Vice President & Controller
Nelson A. Habenicht	Vice President, Marketing
Cheryl L. Lang	Vice President, Human Resources
Gordon S. McLaren	Vice President, Commercial Lines
Paul D. Neuss	Vice President, Information Systems
Paul B. Swank	Vice President, Claims
L. Arnold Chatterton	Vice President, Corporate Automation & Agency Management

### **Appointed Officers**

Theodore R. Olson	Treasurer
Catherine E. Jacoy	Secretary
Francis P. Hogan	Assistant Vice President
William M. Clumpner	Assistant Secretary
Meredith L. Lehr	Director of Corporate Legal Affairs & Assistant Vice President
Ann Marie Davis	Assistant Vice President
Norman E. Donelson	Assistant Vice President
Ralph A. Mill	Assistant Vice President
Joan E. Pierce	Assistant Vice President

Section 4 provides that the Board shall appoint from among its members an Executive Committee composed of not less than three (3) members, including the President and the Chairman of the Board. The Executive Committee shall have full power to act for the Board ad interim.

### **Executive Committee**

Dale E. Abbrederis  
Laurence P. O'Connor - Chairman  
Hans-Rudolf Stucki

### **Investment Committee**

The Investment Committee was discontinued effective February, 1994 when Winterthur took over the Unigard Insurance Group.

## **UNIGARD INSURANCE COMPANY**

### **Conflict of Interest**

The Company has an established conflict of interest procedure for its directors, officers and exempt employees. Each officer and director submits a signed conflict of interest statement to the Corporate Legal Department on an annual basis. Each exempt employee submits a signed conflict of interest statement to the Corporate Legal Department every three years. Any reported exceptions that might be considered conflicts of interest will be reported to the Board of Directors or its Executive Committee. No material exceptions were noted.

### **Minutes**

The examiners reviewed the minutes of the Shareholders, Board of Directors and committees of the Board for the period covered under examination. The Board adequately approved investment transactions. The meetings were well attended.

### **AFFILIATED COMPANIES**

The Company is a wholly owned subsidiary of Unigard, Inc. All of the voting stock of Unigard, Inc., is owned by Winterthur U.S. Holdings, Inc., with its ultimate parent, Winterthur Swiss Insurance Company of Switzerland. As a member of an Insurance Holding Company System, registration statements are required to be filed in accordance with RCW 48.31B.025 and WAC 284-18-300. John Hancock or Winterthur U.S. Holdings, Inc., filed the registration statements for each year under examination on behalf of the Unigard Insurance Group.

The following organization chart is taken in part from the filed 1996 annual statement:

**UNIGARD INSURANCE COMPANY**

(Please refer to hard copy of report on file)

## UNIGARD INSURANCE COMPANY

### **CORPORATE RECORDS**

#### **Contracts/Service Agreements**

On and after December 1, 1993, the Company provides all operating services for Unigard Indemnity Company with reimbursement pursuant to a Service Agreement between the parties dated January 18, 1994. Prior to December 1, 1993, all of the activities and functions of the Company were performed by employees of Unigard Security Insurance Company.

Winterthur Reinsurance Corporation of America, an affiliate, provides all the investment services relating to the Company's assets held in a custody account at the Bank of New York pursuant to the Investment Service Agreement/Asset Management Agreement dated December 10, 1993, as amended June 14, 1995, February 13, 1996, and February 20, 1997. The amendments incorporated by reference revised Investment Policy Guidelines approved by the Company's Board of Directors.

The Company's income tax returns have been consolidated with Winterthur U.S. Holdings, Inc., and its subsidiaries as shown in Schedule Y of the annual statement beginning December, 1993. The method of allocation between the Company, Unigard Indemnity Company, and Unigard, Inc., is subject to a written agreement that was effective on December 10, 1993. The terms and conditions of this agreement require an allocation of taxes based upon separate return calculations resulting in a tax charge or refund of not more than the amount each company would have paid or received if it had filed on a separate return basis.

### **INTERNAL SECURITY**

#### **Fidelity Bonds**

Winterthur U. S. Holdings, Inc., the parent, has a Financial Institution Bond policy that includes coverage for its subsidiaries. The aggregate liability covered by the bond is \$10,000,000.

#### **Other Insurance**

Property and liability coverages are generally provided through a brokerage firm and are primarily underwritten by an appropriate Unigard company, depending on the risks being underwritten. Coverages written on Unigard policies are covered under Unigard's reinsurance program. Excess coverage and other special needs are provided for and underwritten by insurance companies other than those in the Unigard Group.

Winterthur U.S. Holdings, Inc., also has a program of coverages for its subsidiaries for Professional Liability, Directors and Officers Liability, and Fiduciary Liability insurance.

#### **Internal Controls**

The Company retained the firm of Ernst & Young, Certified Public Accountants, to audit its statutory financial statements for the years covered by this examination. The firm issued a report on internal controls as part of the audits with no material weaknesses noted. The examiners also independently tested internal controls and found no material weaknesses.

#### **Internal Audit Function**

The internal audit department for the North American subsidiaries of Winterthur U.S. Holdings, Inc., is located at Republic Financial Services, Inc., in Dallas, Texas, and performs various operational audits to support and supplement the audits of the CPA.

## UNIGARD INSURANCE COMPANY

### Invested Asset Security

Winterthur Reinsurance Corporation of America manages the Company's invested assets held in a custody account at The Bank of New York under an investment service agreement. Examination of the custody agreement with The Bank of New York indicates that proper safeguards are in place to secure the Company's assets.

### OFFICERS AND EMPLOYEES WELFARE AND PENSION PLANS

The Company provides its employees and their dependents with medical, dental, vision care, and life and AD&D benefits. In addition, under Unigard's Pre-Tax Flexible Benefit Plan, employees can take advantage of paying their share of the expense in the plans with pre-tax or tax free dollars.

The Company's employees are eligible to participate in the Company's pension plan; a long term disability plan and a profit sharing savings plan. The Company made adequate provisions in the financial statements for its obligations under these plans.

### TERRITORY AND PLAN OF OPERATION

The Company is authorized to write participating and nonparticipating policies for the following kinds of insurance in Washington: Disability, Property, Marine and Transportation, Vehicle, General Casualty and Surety as defined in RCW 48.11.030 through RCW 48.11.080.

The Company was licensed to operate in the following states as of December 31, 1996:

Alaska	Arizona	California	Colorado
District of Columbia	Idaho	Illinois	Indiana
Louisiana	Massachusetts	Montana	Nevada
New Mexico	New York	North Carolina	North Dakota
Ohio	Oregon	Pennsylvania	Rhode Island
Tennessee	Texas	Utah	Virginia
Washington	West Virginia	Wisconsin	Wyoming

The Winterthur Swiss Group represents the U.S. based operations of Winterthur Swiss Insurance Company, one of the world's largest multiline insurers offering a full array of insurance coverage principally in Europe, North America, Australia and Asia. The group entered the United States in 1936 through the establishment of the United States Branch of the Winterthur Swiss Insurance Company of Winterthur, Switzerland. The parent company, founded in 1875, is one of the largest insurance companies in Switzerland.

The consolidated operations of the U.S. group represent approximately 14% of the Switzerland based parent and are integral to their international insurance strategy. The Winterthur Swiss Group (U.S.) consists of 24 insurance subsidiaries that provide a complete array of property/casualty and life/health products. Property/casualty products are offered by six distinct regional, multiline business units that operate independently of one another. A.M. Best assigns six ratings units as follows:

The first rating unit is based on the consolidation of General Casualty Company of Wisconsin and three affiliates that pool with it. This operation, which generates 33% of Winterthur Swiss' property/casualty net premiums in the U.S., writes a balanced book of personal lines and mainstream commercial lines business largely in the Midwest.

The second rating unit is based on the consolidation of Republic Insurance Company and its seven affiliates. This group, which generates 16% of Winterthur Swiss' net premiums, writes personal lines through independent agents, predominantly in its home state of Texas, and the surrounding eight state area. Commercial business is written for the U.S. operations of international companies insured by the group's ultimate parent, Winterthur Swiss Insurance Company. A majority of this business is then ceded back to the parent and its foreign subsidiaries.

## UNIGARD INSURANCE COMPANY

The third rating unit is based on the operating performance and financial condition of Winterthur Reinsurance Corporation of America, which generates 15% of the Winterthur Swiss Group's net premiums. The company operates as a treaty and facultative reinsurer writing business through brokers, and is among the top fifteen professional reinsurers in the country. The company predominantly underwrites treaty business targeting small-to-medium regional insurers, with approximately 35% of its business generated through a quota share arrangement with the General Casualty Group, an affiliate.

A fourth rating unit is based on the consolidated operating performance and financial condition of Unigard Insurance Company and its subsidiary, UID. The companies, which account for 19% of Winterthur Swiss Group's net premiums, write both commercial and personal lines through independent agents predominantly in the Northwest and Western states.

The fifth rating unit is based on the consolidation of the Southern Guaranty Insurance Company and two subsidiaries that fully reinsure with it, as well as its recently acquired Southern Pilot Group. This operation generates 10% of Winterthur Swiss's property/casualty net premiums by writing homeowners, personal auto, commercial auto and commercial multiple peril insurance primarily in the Southeast.

A sixth rating unit is assigned to Blue Ridge Insurance Group. In 1995, this operation generated approximately 7% of Winterthur Swiss' property/casualty net premium which represents personal lines in the Northeast.

### GROWTH OF COMPANY

The following schedule shows the growth of the Company taken from the filed annual statements and also from the Insurance Department's reports of examination:

<u>Year</u>	<u>Net Premiums Written</u>	<u>Net Losses Paid</u>	<u>Admitted Assets</u>	<u>Surplus as Regards Policyholders</u>
1990*	\$ 11,714,315	\$ 9,804,530	\$ 67,895,114	\$ 39,441,653
1991	8,424,800	8,203,500	66,251,633	43,722,067
1992	9,015,788	7,677,653	65,821,427	46,990,721
1993#	183,381,583	(85,474,283)	421,583,958	109,391,465
1994	219,529,845	128,060,661	460,638,718	148,345,385
1995	224,264,525	139,703,906	482,220,163	166,989,565
1996*	215,397,456	143,034,387	495,211,689	181,982,998
<b>*Per Insurance Department Examination</b>			<b>#Result of the sale to Winterthur in 1993</b>	

### MARKET CONDUCT

The Washington Insurance Department conducted a limited market conduct examination of the Company as of December 31, 1996. The following states conducted full market conduct examinations: California conducted a market conduct examination as of June 9, 1995; North Carolina conducted a market conduct examination as of January 13, 1995, and Illinois conducted a market conduct examination as of December 22, 1995.

The current examination includes a review of personal lines and commercial lines business and the Company's procedures as follows:

#### Treatment of Policyholders

1. Complaints were resolved reasonably.
2. Response to complaints appears to be timely.
3. Complaint logs appear to be properly used.
4. The Company appears to be in compliance with the requirements of the NAIC model act for complaint recording.

# UNIGARD INSURANCE COMPANY

## REINSURANCE

The Company cedes and assumes reinsurance. All reinsurance agreements in effect as of December 31, 1996 were reviewed and the coverage is summarized as follows:

### Reinsurance Ceded

The Company and its subsidiary, Unigard Indemnity Company, are collectively reinsured under a variety of reinsurance treaties. The following schedule summarizes the Companies' ceded reinsurance treaty coverage in force as of December 31, 1996:

<u>Property</u>	<u>Company Retention</u>	<u>Reinsurers' Limits</u>
First Per Risk Excess	\$ 300,000, subject to \$ 375,000 annual aggregate deductible	\$1,200,000 excess of retention, \$3,600,000 per occurrence
Second Per Risk Excess	\$1,500,000	\$3,500,000 excess of retention, \$7,000,000 per occurrence
First Catastrophe Excess	\$ 5,000,000	95% of \$7,500,000 excess of retention, ultimate net loss per occurrence
Second Catastrophe Excess	\$12,500,000	95% of \$7,500,000 excess of retention, ultimate net loss per occurrence
Third Catastrophe Excess	\$20,000,000	95% of \$15,000,000 excess of retention, ultimate net loss per occurrence
Fourth Catastrophe Excess	\$35,000,000	100% of \$15,000,000 excess of retention, ultimate net loss per occurrence
Fifth Catastrophe Excess	\$50,000,000	100% of \$20,000,000 excess of retention, ultimate net loss per occurrence
<u>Casualty</u>	<u>Company Retention</u>	<u>Reinsurers' Limits</u>
First Excess	\$ 500,000 per occurrence, \$ 750,000 aggregate deductible	\$4,500,000 excess \$500,000 per occurrence
Second Excess	\$5,000,000 per occurrence	\$5,000,000 excess \$5,000,000 per occurrence
Workers' Compensation (WC) Gap Excess	\$5,000,000 per occurrence	\$5,000,000 excess \$5,000,000 per occurrence



## UNIGARD INSURANCE COMPANY

Third WC Excess	\$10,000,000 per occurrence	\$10,000,000 excess \$10,000,000 per occurrence
Fourth WC Excess	\$20,000,000 per occurrence	\$42,500,000 excess \$20,000,000 per occurrence
Personal Umbrella Quota Share Automatic Facultative	\$200,000 (20%)	80% First \$1,000,000 100% Next \$4,000,000
Commercial Umbrella QS, Automatic Facultative	\$150,000 (15%)	85% First \$1,000,000 100% Next \$4,000,000
Minimum Premium, Commercial Umbrella QS, Automatic Facultative	\$ 150,000 (15%)	85% First \$1,000,000 100% Next \$4,000,000
Commercial Umbrella Excess	\$5,000,000	\$5,000,000 excess \$5,000,000

### **Reinsurance Assumed**

The Company's reinsurance assumed is derived primarily from its subsidiary, Unigard Indemnity Company, and its former affiliate, Unigard Security Insurance Company.

Unigard Indemnity Company, as part of the intercompany pooling agreement which became effective July 1, 1993, agreed to cede automatically to Unigard Insurance Company all gross liabilities incurred under or in connection with all contracts and policies of insurance issued by the subsidiary. Unigard Insurance Company then retrocedes 14% of this business to Unigard Indemnity Company.

Unigard Security Insurance Company and Winterthur U.S. Holdings, Inc., entered into a stock purchase agreement as of September 24, 1993 which provided for the sale of all the capital stock of Unigard, Inc., the holder of all the issued and outstanding capital stock of Unigard Insurance Company (holder of all the issued and outstanding capital stock of Unigard Indemnity Company).

Under the terms of the Stock Purchase Agreement, the Company and Unigard Indemnity Company entered into a 100% quota share agreement with Unigard Security Insurance Company as of December 10, 1993. The Company agreed to assume "on the terms and conditions and for considerations hereinafter contained, a 100% Quota Share of the Ceding Company's, i.e. Unigard Security Insurance Company's, insurance liabilities and obligations, after reduction for collectible Third Party Reinsurance, and all risks, past, present and future with respect to all business conducted or to be conducted by the Ceding Company but excluding the Excluded Business (the "Business Covered")."

Amendment Number One dated December 31, 1996. states that the agreement "shall continue in full force and effect through December 31, 1997. The parties agreed that the Ceding Company will not write any new business after December 31, 1996."

### **Intercompany Pooling Agreement**

This agreement became effective July 1, 1993 between the Company and Unigard Indemnity Company, its wholly owned property and casualty subsidiary. The reinsurance provided under this agreement is part of an intra-group pooling agreement between affiliated companies and is in excess of any third party reinsurance available to either company. The Company agreed to reinsure and assume, and Unigard Indemnity Company agreed to cede automatically from inception, all gross liabilities of UID incurred under or in connection with all contracts and policies of insurance issued by UID.

## **UNIGARD INSURANCE COMPANY**

The Company and UID agreed that all reinsurance ceded to third party reinsurers should be ceded by UIC. Within this pooling agreement, the Company retains 86% of the “pooled” business and cedes, and/or retro-cedes, 14% to UID.

The Company appears to be in compliance with the Washington Insurance Code and NAIC guidelines regarding authorized and unauthorized reinsurers. The agreements include the insolvency clause in compliance with RCW 48.12.160(2).

### **ACCOUNTING RECORDS AND PROCEDURES**

#### **Accounting Records**

The Company’s accounting functions are processed through accounting software for mainframe computers marketed by McCormick & Dodge and operated on the Company’s computer located at its home office in Bellevue, Washington. Accounting services are also provided through the same program under separate Service Agreements with affiliated and formerly affiliated companies; Unigard, Inc., Unigard Security Insurance Company, Unigard Indemnity Company, Wincorp, Inc. (a Washington corporation), and Wincorp, Inc. (a California corporation).

Companies’ data is entered into the same general ledger program with an identifying company code for separation of each company’s data. The general ledger is maintained on the GL: M system. This system produces a trial balance that is downloaded to a Lotus Spreadsheet for financial reporting. The FREEDOM software is used to prepare the financial pages and exhibits of the NAIC annual statement. Investment accounting for marketable securities is performed using SUNGARD a PC based software package. This system produces the NAIC annual statement investment schedules. Supporting details are recorded in the subsidiary ledgers, journals, and tabulations maintained by the Company’s accounting department.

The Company’s accounting procedures, internal controls and transaction cycles were reviewed during the planning phase of the examination and a trial balance prepared for the year ended December 31, 1996.

#### **Actuarial Opinion**

The actuarial staff of the Insurance Commissioner’s Office reviewed the reserves for the combined companies’ unpaid loss and loss adjustment expenses. The actuarial staff’s estimates indicate that the companies booked reserves for both losses and allocated loss adjustment expenses are in a reasonable range.

### **SUBSEQUENT EVENTS**

On February 18, 1997, the Board of Directors unanimously approved a resolution declaring a cash dividend of \$2,100,000 on the 30,000 shares of common stock of the Company owned by Unigard, Inc., the stockholder of record on the same date. The dividend was paid on March 13, 1997 from the Company’s earned surplus, as defined by RCW 48.08.030(1).

On June 3, 1997, Unigard Insurance Group announced its plans to build four three-story buildings, each with 45,000 square feet of office space and two levels of underground parking on the 47 acres that is home to its corporate headquarters. One building will be occupied by Unigard, and the rest will be leased to one or more tenants. Construction is scheduled to start early next year, with occupancy of the first building set for late 1998.

## **UNIGARD INSURANCE COMPANY**

### **COMMENTS ON RECOMMENDATIONS FROM PREVIOUS EXAMINATION**

The comments and recommendations made in the last examination have been addressed. The OIC's actuary suggested that the required annual report of the Company's pollution reserves filed in the Office of Insurance Commissioner be discontinued.

### **FINANCIAL STATEMENTS**

The following statements present the financial condition of the Company as of December 31, 1996 as determined by this examination.

# BALANCE SHEET

AS OF DECEMBER 31, 1996

	BALANCE PER COMPANY	EXAMINATION ADJUSTMENTS	BALANCE PER EXAMINATION	Notes
<b>ASSETS</b>				
<u>Bonds</u>				
Stocks:	\$317,076,263		\$317,076,263	1
Mortgage loans on real estate	85,891,605		85,891,605	2
Real estate:	2,890,118		2,890,118	3
Properties occupied by the company			0	
Other properties	23,633,409		23,633,409	4
Collateral loans	779,062		779,062	
Short-term investments	(5,346,065)		(5,346,065)	
Other invested assets	17,055,405		17,055,405	
Aggregate write-ins for invested assets	849,969		849,969	
Agents' balances or uncollected premiums:	2,579,000		2,579,000	
Premiums in course of collection less ceded reinsurance			0	
Premiums booked but deferred and not yet due	16,939,801		16,939,801	
Accrued retrospective premiums	19,340,309		19,340,309	
Bills receivable, taken for premiums	1,228,300		1,228,300	
Federal income tax recoverable	2,314,857		2,314,857	
Electronic data processing equipment	785,950		785,950	5
Interest, dividends and real estate income due and accrued	3,009,671		3,009,671	
Receivable from parent, subsidiaries and affiliates	5,142,094		5,142,094	
Equities and deposits in pools & associations	863,529		863,529	
Total Assets	178,412		178,412	
	<u>\$495,211,689</u>	<u>\$0</u>	<u>\$495,211,689</u>	
<b>LIABILITIES</b>				
Losses	\$180,173,150		\$180,173,150	
Loss adjustment expenses	28,177,036		28,177,036	
Contingent commissions and other charges	2,179,444		2,179,444	
Other expenses (excluding taxes, licenses & fees)	8,160,952		8,160,952	
Taxes, licenses & fees (excl. fed. inc. tax)	299,171		299,171	
Unearned premiums	89,079,746		89,079,746	
Funds held by company under reinsurance treaties	86,723		86,723	
Amounts withheld by company for others	440,522		440,522	
Provision for reinsurance	703,091		703,091	
Excess of statutory reserves over statement reserves	1,825,000		1,825,000	
Drafts outstanding	1,254,499		1,254,499	
Aggregate write-ins for liabilities	849,357		849,357	
Total liabilities	313,228,691	0	313,228,691	
<b><u>SURPLUS AND OTHER FUNDS</u></b>				
Common capital stock	3,000,000		3,000,000	
Gross paid in and contributed surplus	119,053,571		119,053,571	
Unassigned funds (surplus)	59,929,427		59,929,427	
Surplus as regards policyholders	181,982,998	0	181,982,998	
Total liabilities, surplus and other funds	<u>\$495,211,689</u>	<u>\$0</u>	<u>\$495,211,689</u>	

# UNIGARD INSURANCE COMPANY

## STATEMENT OF INCOME

YEAR ENDED DECEMBER 31, 1996

	BALANCE PER COMPANY	EXAMINATION ADJUSTMENTS	BALANCE PER EXAMINATION	Notes
<u>UNDERWRITING INCOME</u>				
Premiums earned	\$215,834,790		\$215,834,790	
DEDUCTIONS:				
Losses incurred	147,567,664		147,567,664	
Loss expenses incurred	19,606,079		19,606,079	
Other underwriting expenses incurred	64,520,718		64,520,718	
Total underwriting deductions	231,694,461	0	231,694,461	
Net underwriting gain or (loss)	(15,859,671)	0	(15,859,671)	
<u>INVESTMENT INCOME</u>				
Net Investment Income earned	22,171,875		22,171,875	
Net realized capital gains or (losses)	5,763,911		5,763,911	
Net investment income gain or (loss)	27,935,786	0	27,935,786	
<u>OTHER INCOME</u>				
Net gain or loss				
from agents' or premium balances charged off	(253,859)		(253,859)	
Finance and service charges				
not included in premiums	1,645,488		1,645,488	
Miscellaneous interest income	178,333		178,333	
Total other income	1,569,962	0	1,569,962	
Net income before dividends to policyholders and before federal and foreign income taxes	13,646,077	0	13,646,077	
Dividends to policyholders	821,265		821,265	
Net income before federal and foreign income taxes	12,824,812	0	12,824,812	
Federal and foreign income taxes incurred	2,424,354		2,424,354	
Net income	\$10,400,458	\$0	\$10,400,458	

## CAPITAL AND SURPLUS ACCOUNT

AS OF DECEMBER 31, 1996

Surplus as regards policyholders, December 31, previous year	\$166,989,565		\$166,989,565
<u>GAINS AND (LOSSES) IN SURPLUS</u>			
Net income	10,400,458	0	10,400,458
Net unrealized capital gains or (losses)	5,455,117		5,455,117
Change in non-admitted assets	143,858		143,858
Change in provision for reinsurance	(19,068)		(19,068)
Change in excess of statutory reserves over statement reserves	(1,006,000)		(1,006,000)
Reserve for potential losses on uncollectible reinsurance balances	19,068		19,068
Changes in surplus	14,993,433	0	14,993,433
Surplus as regards policyholders, December 31, current year	\$181,982,998	\$0	\$181,982,998

# UNIGARD INSURANCE COMPANY

## COMPARATIVE BALANCE SHEET AS OF DECEMBER 31,

	<u>1996</u>	<u>1995</u>
<u>ASSETS</u>	<u>0</u>	
Bonds	\$317,076,263	\$319,988,957
Common stocks	85,891,605	68,028,761
Mortgage loans on real estate	2,890,118	3,778,396
Real estate:	0	
Properties occupied by the company	23,633,409	23,483,122
Other properties	779,062	586,344
Cash on hand and on deposit	(5,346,065)	(5,814,256)
Short-term investments	17,055,405	22,538,085
Other invested assets	849,969	317,371
Aggregate write-ins for invested assets	2,579,000	1,901,418
Agents' balances or uncollected premiums:	0	
Premiums in course of collection less ceded reinsurance	16,939,801	21,143,719
Premiums booked but deferred and not yet due	19,340,309	16,611,879
Funds held by or deposited with reinsured companies	1,228,300	
Reinsurance recoverable on loss & loss adj. expense pmts.	2,314,857	2,474,586
Federal income tax recoverable	785,950	
Electronic data processing equipment	3,009,671	527,791
Interest, dividends and real estate income due and accrued	5,142,094	5,443,415
Receivable from parent, subsidiaries and affiliates	863,529	967,123
Aggregate write-ins for other than invested assets	178,412	243,452
Total Assets	<u>\$495,211,689</u>	<u>\$482,220,163</u>
<u>LIABILITIES</u>		
Losses	\$180,173,150	\$175,639,873
Loss adjustment expenses	28,177,036	33,694,799
Contingent commissions and other charges	2,179,444	3,475,895
Other expenses (excluding taxes, licenses & fees)	8,160,952	9,068,697
Taxes, licenses & fees (excl. fed. inc. tax)	299,171	331,826
Unearned premiums	89,079,746	89,517,081
Funds held by company under reinsurance treaties	86,723	82,042
Amounts withheld by company for others	440,522	307,029
Provision for reinsurance	703,091	684,023
Excess of statutory reserves over statement reserves	1,825,000	819,000
Drafts outstanding	1,254,499	627,012
Aggregate write-ins for liabilities	849,357	868,425
Total liabilities	<u>313,228,691</u>	<u>315,230,598</u>
<u>SURPLUS AND OTHER FUNDS</u>		
Common capital stock	3,000,000	3,000,000
Gross paid in and contributed surplus	119,053,571	119,053,571
Unassigned funds (surplus)	59,929,427	44,935,994
Surplus as regards policyholders	181,982,998	166,989,565
Total liabilities, surplus and other funds	<u>\$495,211,689</u>	<u>\$482,220,163</u>

# UNIGARD INSURANCE COMPANY

## COMPARATIVE STATEMENT OF INCOME FOR THE YEARS ENDED DECEMBER 31,

	1996	1995
<u>UNDERWRITING INCOME</u>		
Premiums earned	\$215,834,790	\$221,426,235
DEDUCTIONS:		
Losses incurred	147,567,664	144,655,692
Loss expenses incurred	19,606,079	21,792,296
Other underwriting expenses incurred	64,520,718	69,218,964
Total underwriting deductions	231,694,461	235,666,952
Net underwriting gain or (loss)	(15,859,671)	(14,240,717)
<u>INVESTMENT INCOME</u>		
Net Investment Income earned	22,171,875	22,633,149
Net realized capital gains or (losses)	5,763,911	4,570,525
Net investment income gain or (loss)	27,935,786	27,203,674
<u>OTHER INCOME</u>		
Net gain or loss	0	
from agents' or premium balances charged off	(253,859)	(290,646)
Finance and service charges	0	
not included in premiums	1,645,488	1,704,051
Miscellaneous interest income	178,333	219,066
Total other income	1,569,962	1,632,471
Net income before dividends to policyholders and before federal and foreign income taxes	13,646,077	14,595,428
Dividends to policyholders	821,265	1,041,177
Net income before federal and foreign income taxes	12,824,812	13,554,251
Federal and foreign income taxes incurred	2,424,354	5,474,104
Net income	\$10,400,458	\$8,080,147

## COMPARATIVE CAPITAL AND SURPLUS ACCOUNT AS OF DECEMBER 31,

	1996	1995	1994	1993	1992
Surplus as regards policyholders, December 31, previous year	\$166,989,565	\$148,345,384	\$109,391,465	\$46,990,719	\$43,722,067
<u>GAINS AND (LOSSES) IN SURPLUS</u>					
Net income	10,400,458	8,080,147	12,476,713	1,988,220	2,036,187
Net unrealized capital gains or (losses)	5,455,117	10,488,313	(769,842)	(192,906)	265,465
Change in non-admitted assets	143,858	(287,858)	1,533,111	(4,534,702)	
Change in provision for reinsurance	(19,068)	121,897	762,912	(1,568,832)	
Change in excess of statutory reserves over statement reserves	(1,006,000)	(819,000)			967,000
Capital changes	0			500,000	
Surplus adjustments	0		25,000,000	65,571,508	
Reserve for potential losses on uncollectible reinsurance balances	19,068	1,060,682	(48,975)	637,458	
Changes in surplus	14,993,433	18,644,181	38,953,919	62,400,746	3,268,652
Surplus as regards policyholders, December 31, current year	\$181,982,998	\$166,989,565	\$148,345,384	\$109,391,465	\$46,990,719

# UNIGARD INSURANCE COMPANY

## NOTES TO FINANCIAL STATEMENTS

### **1. Bonds**

Bonds, not backed by other loans, are valued at lower of amortized cost or investment value based on the NAIC Valuation of Securities. Discount or premium on bonds is amortized using the effective interest method. For loan-backed bonds, anticipated prepayments at the date of purchase are considered when determining the amortization of discount or premium. There have been no significant changes in estimated cash flows from the original purchase assumptions.

### **2. Common Stocks**

Common stocks of unaffiliated companies are reported at market as determined by the NAIC Valuation of Securities. Common stocks of affiliated companies are reported at the affiliated company's net statutory equity, with the change in equity reflected as a direct credit or charge to unassigned surplus.

### **3. Mortgage Loans on Real Estate**

Mortgage loans on real estate are stated at the aggregate unpaid balance. Fire insurance is required on all properties covered by mortgage loans. This insurance is at least equal to the excess of the loan over the maximum loan that would be permitted by law on the land without the buildings.

### **4. Real Estate**

The Company uses the straight-line method of depreciation for all real estate owned and occupied over the estimated useful lives of the properties. Investment income and operating expense include rent for the Company's occupancy of those properties. Land is reported at cost and other real estate is reported at depreciated cost.

### **5. Federal Income Tax Allocation**

The Company's operations are consolidated with Unigard, Inc. and its subsidiaries, which is included in a consolidated federal income tax return with Winterthur U.S. Holdings, Inc. and all its subsidiaries. The method of allocation of taxes is subject to a written agreement with Unigard, Inc. The allocation of taxes is based upon separate return calculations resulting in a tax charge or refund of not more than the amount each company would have paid or received if it had filed on a separate return basis. If, on the basis of separate return calculations, a subsidiary would be entitled to refunds of federal income taxes, Unigard, Inc. will pay to the subsidiary an amount equal to the refunds that the subsidiary would have received from the Internal Revenue Service.

### **6. Loss and Loss Adjustment Expense Reserves**

These liabilities represent the estimated ultimate net cost of all reported and unreported losses incurred but not paid through the end of the year. The unpaid losses and loss adjustment expenses, which are not discounted except for tabular discounts on workers' compensation claims, and include anticipated salvage and subrogation recoveries, are estimated using individual case-basis valuations and statistical analyses as required by the Insurance Department.

### **7. Unearned Premiums**

The Company's total unearned premium reserve represents the unearned premium liability for all policies in force. At the expiration of an insurance contract or policy, the entire premium has been earned. At any point prior to expiration, the Company is required to establish a pro rata portion of the premium as a liability to cover the remaining policy term.



## UNIGARD INSURANCE COMPANY

### COMMENTS ON FINANCIAL STATEMENTS

#### Bonds

**\$317,076,263**

The Company's investment in bonds represents 64% of total admitted assets as of December 31, 1996. The bond portfolio consisted of the following:

<u>Classification</u>	<u>Statement Value</u>	<u>Par Value</u>	<u>Market Value</u>
U.S. Government	\$195,761,047	\$186,145,000	\$190,754,450
Industrial & Misc.	<u>121,315,216</u>	<u>120,000,000</u>	<u>120,315,056</u>
Total	<u>\$317,076,263</u>	<u>\$306,145,000</u>	<u>\$311,069,506</u>

The Company uses the effective yield method to amortize bond premiums and discounts. Premiums and discounts on bonds classified as other than collateralized mortgage obligations are amortized in accordance with the NAIC Annual Statement Instructions manual. Collateralized mortgage obligation bond premiums and discounts are accounted for as prescribed by FASB 91, which requires that amortization be accelerated when prepayments of principal are received. The testing of amortized values to maturity in accordance with the NAIC Examiners Handbook revealed no material differences.

#### Agents' Balances or Uncollected Premiums

**\$36,280,110**

Although the total premium receivable shown on the sub-lines of annual statement Line 10 are correct, the amounts shown on sub-lines 10.1 and 10.2 are based on the Company's estimated allocation of the total. In the 1995 annual statement, \$14,137,184 of the \$16,611,879 reported was estimated. The Company should have booked the actual amount rather than an estimated balance in accordance with NAIC annual statement instructions.

#### Losses and Loss Adjustment Expenses

**\$208,350,186**

The reserves for the combined companies' unpaid loss and loss adjustment expenses were reviewed by the casualty actuarial staff employed by the Insurance Commissioner's Office. Company personnel provided loss and allocated loss adjustment expense development data by line of business, as well as additional information. Actuarial staff also reviewed actuarial reports prepared by the companies' consulting actuarial firm, Tillinghast, a Towers Perrin Company.

The actuarial staff's estimates indicate that the companies' booked reserves for both losses and allocated loss adjustment expenses are in a reasonable range. Actuarial staff also concluded that the companies' methods of establishing bulk and IBNR reserves, including reserves for unallocated loss adjustment expenses, are reasonable. Therefore, the reserves carried by the companies are accepted as they appear on the companies' 1996 Annual Statements.

## **UNIGARD INSURANCE COMPANY**

### **ACKNOWLEDGMENT**

The cooperation and assistance of the officers and employees of the Company during the examination are hereby acknowledged.

In addition, Timoteo L. Navaja, CFE, CIE, Examiner in Charge, Peter M. Mendoza, CFE, CIE, Larry A. Omdal, Martin Severeid, CIE and D. Lee Barclay, FCAS, MAAA, Actuary and Joshua Ligosky all from the Washington Insurance Commissioner's Office, participated in the examination and preparation of this report.

**UNIGARD INSURANCE COMPANY**

**AFFIDAVIT OF EXAMINER IN CHARGE**

**STATE OF WASHINGTON)**

**) ss**

**COUNTY OF KING )**

TIMOTEO L. NAVAJA, being duly sworn, deposes and says that the foregoing report subscribed by him is true to the best of his knowledge and belief.

He attests that the examination of Unigard Insurance Company was performed in a manner consistent with the standards and procedures required or prescribed by the Washington Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).

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TIMOTEO L. NAVAJA, CFE, CIE  
Examiner in Charge  
State of Washington

Subscribed and sworn to before me on this 4th day of December, 1997.

Colleen Jansen  
Notary Public in and for the State  
of Washington, residing at Seattle.